

Motor Vehicle Fuel Tax Law
(Title 18, Division 2, Chapter 1 of the California Code of Regulations)
Adopt regulations 1123, 1124, 1161 and 1178;
Amend regulations 1101, 1105, 1120, 1132, and 1134; and
Repeal regulations 1103, 1104, 1106, 1107, 1108, 1114, 1115, 1116, 1117, 1118, 1110, 1121,
1131, 1133, 1151, 1152, 1153, 1154, 1155, 1171, 1172, 1173, 1174, 1175, and 1176;
and
Diesel Fuel Tax Law
(Title 18, Division 2, Chapter 3 of the California Code of Regulations)
Adopt regulations 1435 and 1436;
Amend regulations 1420, 1422, and 1430.

REVISED FINAL STATEMENT OF REASONS

Update

On March 27, 2002, the Board adopted Motor Vehicle Fuel Tax Law Regulations 1123, 1124, 1161, and 1178 and Diesel Fuel Tax Law Regulations 1435 and 1436; the Board amended Motor Vehicle Fuel Tax Regulations 1101, 1105, 1120, 1131, and 1134 and Diesel Fuel Tax Law Regulations 1420, 1422, and 1430; and the Board repealed Motor Vehicle Fuel Tax law Regulations 1103, 1104, 1106, 1107, 1108, 1114, 1115, 1116, 1117, 1118, 1119, 1121, 1131, 1133, 1151, 1152, 1153, 1154, 1155, 1171, 1172, 1173, 1174, 1175, and 1176.

During the course of preparing the proposed regulations, and prior to the publication of the proposed regulations under the Administrative Procedures Act (APA), the Board sought the advice and input of interested parties at public meetings held on August 9, 2001, September 20, 2001, and November 28, 2001. The suggestions and comments made by the interested parties during the drafting stages of the regulations were incorporated into the regulations before the APA Notice of Public Hearing, and no written or oral comments were received during the APA comment period, or at the hearing.

Regulation 1101 Defines Motor Vehicle Fuel.

Existing Regulation 1101 is proposed to be amended to reflect changes in the definitions of motor vehicle fuel and other kinds of fuel under the Motor Vehicle Fuel Tax Law that took effect on January 1, 2002. For the most part, those definitions in state law track the definitions which are in use in federal law. Since the persons subject to Motor Vehicle Fuel Tax are also subject to federal excise tax on fuel, it is appropriate to adopt definitions which are consistent with the federal definitions for ease of administration and compliance.

The new definition of motor vehicle fuel is found in part in several sections of the Revenue and Taxation Code. The proposed regulation places the various components of the definition in one place. Also, the proposed regulation identifies what is not motor vehicle fuel.

For example, the law identifies gasoline blendstocks as a petroleum product component of gasoline and includes them in the definition of motor vehicle fuel. The proposed regulation at 1101(f)(1) clarifies that definition by listing the products that are gasoline blendstocks and, like the Internal Revenue Service Regulation (26 CFR 48.4081-1), at 1101(f)(2) clarifies what is not a gasoline blendstock.

Similarly, the law generally defines aviation gasoline and finished gasoline. Proposed regulation 1101(b) tracks the Internal Revenue Service definition in adding industry-recognized specifications (26 CFR 48.4081-1). Likewise, proposed regulation 1101(c) tracks the Internal Revenue Service definition of finished gasoline (26 CFR 48.4081-1).

Racing fuel is formulated specifically for use off the highway, and off-highway use is not subject to tax. Under the proposed regulation, "racing fuel" is excluded from the definitions of motor vehicle fuel at 1101(a) and blended motor vehicle fuel at 1101(g) so that it can be removed at the rack without the imposition of motor vehicle fuel tax. During the initial drafting stages of the regulations, and prior to the APA notice period, the objective was to clearly describe racing fuel in a manner that would distinguish it from taxable motor vehicle fuel. Industry representatives suggested that the racing fuel definition be divided into leaded racing fuel and unleaded racing fuel. Leaded racing fuel is defined in subdivision (h)(1) to mean fuel that (i) generally is used in vehicles not eligible to be registered for highway use, and (ii) is not diesel fuel, kerosene or gasoline blendstock, and (iii) has an octane rating of 100 or higher, and (iv) contains 1.0 gram of lead per gallon or more, and (v) does not meet the ASTM specification for gasoline. Unleaded racing fuel is defined in subdivision (h)(2) to mean fuel that (i) is not diesel fuel, kerosene or gasoline blendstock, and (ii) has an octane rating of 100 or higher, and (iii) does not meet California Air Resources Board specification for gasoline.

Regulation 1105 Defines Tax-Paid Fuel and Ex-Tax Fuel.

Existing regulation 1105(a) defines "tax-paid fuel" and "ex-tax fuel" and existing regulation 1105(b) provides that a distributor or broker who acquires tax-paid fuel from a licensed motor vehicle fuel distributor or broker is not liable for tax on the tax-paid gallons, that a distributor who fails to invoice or collect tax on a taxable distribution remains liable for the tax, and that a distributor who distributes ex-tax fuel to a qualified distributor and indicates that the fuel is tax-paid remains liable for tax on that fuel.

Under the Motor Vehicle Fuel Tax Law that took effect on January 1, 2002, tax is imposed on a supplier upon removal, entry, or sale of motor vehicle fuel instead of on the distribution by a distributor or broker. Therefore, on and after January 1, 2002, it is no longer necessary to explain the continuing tax liability of a distributor upon distribution of fuel. For that reason, the existing 1105(b) is proposed to be repealed. The terms "tax-paid fuel" and "ex-tax fuel" are proposed to be defined at 1105(a) and 1105(b) respectively and other minor clarifying changes are proposed to be made to those definitions. In addition, at 1105(a)(2) a purchase receipt which shows that tax was included in the amount a purchaser paid for the motor vehicle fuel is listed as the type of documentation which supports a claim that fuel is tax-paid. The proposed regulation is nearly identical to existing Board Regulation 1413, which pertains to the Diesel Fuel Tax Law.

Regulations 1120 and 1436, Returned Sales and Invoice Corrections.

Statutory changes effective January 1, 2002, necessitated that Regulation 1120 be amended in several respects. First, since under the new law, tax is imposed at the time the fuel is removed from the refinery or terminal rack, if the fuel is placed in storage above the rack after its initial removal, entry or sale, it will be taxed a second time when it is subsequently removed from the rack. To avoid double taxation of the fuel, it is necessary to establish a procedure for claiming a credit or refund on returned fuel. The regulation explains that when motor vehicle fuel is returned to a refinery or an approved terminal by the supplier, the supplier can avoid paying tax a second time on the same fuel by either filing a claim for refund with the State Controller or taking a credit on the supplier's tax return filed with the Board. The result is that when the fuel is subsequently removed at the rack, the supplier will be taxed in the normal course. Because the supplier was credited or refunded the tax it paid on the first removal, entry or sale of the returned fuel, and paid the tax on the second removal, the supplier only pays tax one time on the fuel.

Proposed subdivision (a) substitutes the defined term "supplier" for "distributor" and clarifies how a supplier is to handle motor vehicle fuel returned by a customer.

Proposed subdivision (b) of the regulation presumes (i) that the supplier purchased the motor vehicle fuel tax-paid if the credit memorandum includes motor vehicle fuel tax and (ii) that for purposes of a refund or credit, the supplier subsequently removed the motor vehicle fuel from a refinery or terminal rack in the same month that the motor vehicle fuel was returned.

Proposed subdivision (c) clarifies that the credit will be allowed on the supplier's tax return only if the following conditions are met: (i) the returned fuel is delivered into a refinery or an approved terminal, (ii) the credit is taken on a tax return filed with the Board within three months after the close of the calendar month in which the motor vehicle is returned, (iii) the supplier prepares a First Taxpayer's Report on the returned fuel, and (iv) a copy of the First Taxpayer's Report and credit memorandum are retained for inspection by the Board with the tax return.

Proposed subdivision (d) clearly states that if a supplier fails to claim a credit in the specified manner, it may only file a claim for refund with the State Controller to recover the tax. The regulation lists the information and documentation that is required to be included in the claim for refund. Also, the claim must be filed within three years from the date of return of the fuel.

Existing subdivision (b), which deals with invoice correction, is repealed because the record keeping requirements are covered in Regulation 1178, Records.

The diesel fuel Regulation 1436 is a new regulation, which provides that when diesel fuel is returned to the supplier by a customer and delivered into a refinery or an approved terminal, the supplier may either file a claim for refund of the tax with the Board or take a credit on the supplier's tax return filed with the Board. The regulation explains when and how the credit may

be taken and when a refund must be filed. The regulation is identical to Regulation 1120 except that the regulation explains that the claim for refund of the diesel fuel tax must be filed with the Board, rather than with the State Controller.

Regulations 1123 and 1420, Supplier.

Effective January 1, 2002, Section 7338 of the Revenue and Taxation Code defined the term "supplier" to include blenders, enterers, position holders, refiners, terminal operators, and throughputters. The proposed regulation identifies the various types of motor vehicle fuel suppliers and describes the imposition of the motor vehicle fuel tax and the reporting requirements of each. The proposed regulation also describes the circumstances in which the terminal operator is jointly liable with a supplier for the removal of motor vehicle fuel from the terminal rack. The proposed regulation is nearly identical to the Board's existing Diesel Fuel Tax Regulation 1420.

Revenue and Taxation Code Section 60203 required that a diesel fuel throughputter file a separate tax return. That code section was repealed effective January 1, 2002. Therefore, the last sentence in existing Regulation 1420 (a) is being dropped since it refers to a separate throughputter return.

Regulations 1124 and 1422, Relief From Liability.

Effective January 1, 2002, the Motor Vehicle Fuel Tax Law, Section 7657.1, of the Revenue and Taxation Code, provided that a taxpayer may be relieved of liability from the Motor Vehicle Fuel Tax, including penalty and interest, if the Board finds that the person's failure to make a timely return or payment was due to the person's reasonable reliance on written advice from the Board. Regulation 1124 is proposed to clarify the circumstances under which relief may be granted for reliance on written advice of the Board. The proposed regulation is nearly identical to the Board Regulation 1705, which pertains to the Sales and Use Tax Law.

Existing Diesel Fuel Tax Law Regulation 1422 is being revised to conform to Sales and Use Tax Regulation 1705 and to proposed Motor Vehicle Fuel Tax Regulation 1122. The proposed changes include written advice in the form of an annotation or legal ruling of counsel under the conditions set forth in new subdivision (d). Also, new subdivision (e) adds that a trade or industry association requesting advice for its members must identify the member for whom the advice is requested in order for the relief from liability to apply. These revisions make Regulation 1422 nearly identical to the other Board regulations on relief from liability.

Discussion of Regulations 1132 and 1430, Shipments Out of the State.

As a result of the statutory changes that became effective January 1, 2002, Regulation 1132 is proposed to be amended to replace references to "distributor" with references to "supplier". The existing regulation provides that stock transfers of ex-tax fuel to a point outside California are not distributions and therefore are not subject to tax. With the changes in point of imposition of tax that took effect January 1, 2002, this instruction is no longer relevant.

Therefore, the language pertaining to stock transfers is proposed to be deleted from subdivisions (c) and (d).

The proposed regulation is nearly identical to the existing Board Regulation 1430, which pertains to the Diesel Fuel Tax Law, except that the time for taking a credit or filing a claim for refund has been amended to be the same in both Regulation 1430 and Regulation 1132.

During the drafting of the proposed regulations, prior to APA notice and hearing, interested parties from the fuel industry had expressed a concern about the requirement that exports be supported by a written contract requiring the supplier to deliver fuel out of the state in order to qualify for exemption from tax. After reviewing the law, industry and staff agreed that a statutory change would be required to remove the requirement for an underlying written export contract.

Discussion of Regulation 1134, Sales to the United States.

The first two paragraphs of existing Regulation 1134 were, in the proposed regulation designated as subdivision (a) and within that subdivision, references to "distribution" and "distributor" were replaced with "sales" and "seller" to conform to the definitions in the law which became effective on January 1, 2002. Subdivision (b) was added to clarify that a supplier making a sale of ex-tax fuel to the United States armed forces may claim an exemption on the supplier's tax return. Subdivision (c) was added to clarify that any person making a sale of tax-paid fuel to the United States armed forces shall file a claim for refund of the tax with the State Controller.

The remainder of the existing regulation is proposed to be repealed as no longer necessary since Revenue and Taxation Code Sections 7401, 7486 and 7487 (relating to exemptions for distributors and brokers and to bond requirements of distributors and brokers) were repealed effective January 1, 2002.

Regulations 1161, Tax Paid Twice on Motor Vehicle Fuel, and 1435, Tax Paid Twice on Diesel Fuel.

A supplier is required to pay tax on the removal from a terminal rack of motor vehicle fuel or diesel fuel. On infrequent occasions, a supplier may need to remove motor vehicle fuel or diesel fuel from one terminal rack and transport it to another terminal to be stored above the rack. This may occur when one part of the state has a shortage of fuel due to a pipeline delivery problem. A subsequent removal of that fuel from the rack will be a removal of fuel on which a prior tax was paid. The process for obtaining a credit or refund of tax when tax is removed from the rack for a second time is outlined in Regulation 1161 for motor vehicle fuel tax and Regulation 1435 for diesel fuel tax. For ease of administration by the Board and for ease of compliance by the taxpayer, the process set forth in the regulation is based on the similar process in place for credits and refunds under federal law which applies to both motor vehicle fuel and diesel fuel taxes. The First Taxpayer's Report and Second Taxpayer's Report are patterned after the forms adopted by the Internal Revenue Service. (See 26 CFR 48.4081-7)

Under Regulation 1161, when a supplier removes motor vehicle fuel from a rack on which a prior tax was paid, the supplier may either file a claim for refund of the “second” tax with the State Controller or take a credit on the supplier's tax return for the “second” tax. The regulation explains when and how the credit may be taken and when and how a refund claim must be filed. (The same is true for diesel fuel, except that the claim for refund would be filed with the Board, not the Controller.) The regulation defines a first taxpayer as the person paying to the State the first tax on the fuel and defines a second taxpayer as the person paying to the State the second tax on the fuel.

The proposed regulation includes the following:

- (1) Subdivisions (b)(3) and (d) of Motor Vehicle Fuel Tax Regulation 1161 requires that the tax paid twice credit be taken on a tax return filed within three months after the close of the calendar month in which the second tax was reported to the state. This time within which to claim a credit in lieu of refund is the same as in Regulations 1120 and 1436.
- (2) Subdivisions (b)(5) and (c)(1) of Motor Vehicle Fuel Tax Regulation 1161 requires that a First Taxpayer's Report must be retained for inspection by the Board with the tax return on which the supplier claimed the credit. A credit may be taken on a supplier's tax return. The regulation explains that the second taxpayer must take the credit on a tax return filed within three months after the close of the calendar month in which the second taxpayer pays the second tax by reporting the gallons on its tax return. The first taxpayer must have paid the first tax by reporting the gallons on its tax return. Also, the first taxpayer must not have received a credit or refund of the first tax.

Regulation 1161 explains when a First Taxpayer's Report must be retained and to whom a copy of the report must be given. The regulation explains that when a person receives a First Taxpayer's Report and subsequently sells the fuel, the person must give a copy of the First Taxpayer's Report and a Statement of Subsequent Seller to the buyer. The regulation contains a model of the First Taxpayer's Report and the Statement of Subsequent Seller that outlines the information required. The model report and statement contain all the items of the Federal models plus some specific state items.

With respect to a claim for refund of motor vehicle fuel tax, Regulation 1161 provides that the claim must be filed with the State Controller in those cases when the credit is not taken on a supplier's tax return filed with the Board within three months after the close of the calendar month in which the second tax gallons were reported. (Unlike motor vehicle fuel tax claims for refund, diesel fuel tax claims for refund are required to be filed with the Board.) Regulation 1161 explains the information to be included in the claim for refund and that a copy of the First Taxpayer's Report and Statement of Subsequent Seller must be attached. Also, the claim for refund must be filed within three years from the date of purchase of the fuel.

Regulation 1435 is proposed to be added regarding diesel fuel. When a supplier is required to pay tax on the removal from the terminal rack of diesel fuel on which a prior tax was paid , the supplier may either file a claim for refund of the tax with the Board or take a credit on

the supplier's tax return filed with the Board. Regulation 1435 explains when and how the credit may be taken and when a refund claim must be filed. The regulation is nearly identical to Regulation 1161 except that the regulation explains that the claim for refund of the diesel fuel tax is to be filed with the Board. As under Regulation 1161, the process for obtaining a credit or refund of tax on diesel fuel under Regulation 1435 is patterned on the federal procedure, and the use of the First Taxpayer's Report and Second Taxpayer's Report. (See Internal Revenue Regulation at 26 CFR 48.4081-7.)

Regulation 1178, Records.

Effective January 1, 2002, the Motor Vehicle Fuel Tax Law, Sections 8253, 8301, 8302 and 8303, of the Revenue and Taxation Code, provided that a taxpayer must maintain and make available records and source documentation in such form as the Board may require. The proposed regulation specifies the records and documentation that are necessary and the form in which they should be maintained in order to support reported amounts. Since many businesses use automated data processing systems and reproductions from microfilm and microfiche, the proposed regulation stipulates the required form and content for automated records and reproductions from microfilm and microfiche. The proposed regulation informs taxpayers how long records must be retained and provides that records must be made available for the Board's examination during that time. Since failure to maintain and keep complete and accurate records may be considered evidence of negligence or intent to evade the tax, the proposed regulation informs taxpayers that such failure may result in penalties or other administrative action. The proposed regulation is nearly identical to the existing Board Regulation 1698, which pertains to the Sales and Use Tax Law.

Discussion of Motor Vehicle Fuel Tax Regulations to be Repealed.

Effective January 1, 2002, Chapter 1053, Statutes of 2000, (AB 2114) changed the definitions, imposition of tax and exemptions in the Motor Vehicle Fuel Tax Law. Also, the sections of the Motor Vehicle Fuel Tax Law dealing with returns and records were repealed or amended. As a result of these statutory changes the twenty-five Motor Vehicle Fuel Tax regulations listed below are obsolete, and should be repealed:

- Regulation 1103, Blending or Compounding;
- Regulation 1104, Consignment for Sale;
- Regulation 1106, Tax-Paid Fuel Distributed;
- Regulation 1107, Drip Gasoline Producer;
- Regulation 1108, Qualified Distributor;
- Regulation 1114, Book Transfers, In-Tank Transfers, Physical Exchanges and Settlements;
- Regulation 1115, Pipeline Overages and Shortages;
- Regulation 1116, Losses Prior to Distribution;
- Regulation 1117, Allowable Losses of Commission Agents;
- Regulation 1118, Distribution of Commingled Fuel;
- Regulation 1119, Tax-Paid Motor Vehicle Fuel Blended, Compounded or Redistilled;
- Regulation 1121, Temperature Corrected Distributions;

Regulation 1131, Natural Gasoline Sales to Licensed Distributors;
Regulation 1133, Exempt Distributions to a Qualified Distributor;
Regulation 1151, Monthly Return of Distributor;
Regulation 1152, Weekly Return of Distributor;
Regulation 1153, Processor's Return of Distribution;
Regulation 1154, Owner's Return of Processing Transactions;
Regulation 1155, Recipient's Return of Processing Transactions;
Regulation 1171, Distributor's Inventory and Stock Record;
Regulation 1172, Producer's Stock Record;
Regulation 1173, Producer's Purchase Record;
Regulation 1174, Producer's Sales Record;
Regulation 1175, Broker's Purchase Record; and
Regulation 1176, Broker's Sales Record.

Cost to Local Agencies and School Districts.

The State Board of Equalization has determined that the proposed regulations do not impose a mandate on local agencies or school districts. Further, the Board has determined that the regulations will result in no direct or indirect cost or savings to any State agency, any local agency or school district that is required to be reimbursed under Part 7 (commencing with section 17500) of Division 4 of Title 2 of the Government Code or other non-discretionary cost or savings imposed on local agencies, or cost or savings on Federal funding to the State of California.

Alternatives Considered.

The Board has determined that no alternative considered would be more effective in carrying out the purpose for which this action is proposed or be as effective and less burdensome to affected private persons than the proposed action.

Responses to Public Comments.

There were no public comments at the Public Hearing held on March 27, 2002, and there were no written comments received from the APA Notice period to the end of the comment period on the regulations discussed herein, and they were adopted, amended and repealed as published.

Board Finding Re Reports.

The Board finds in amending and adopting the regulations described herein, that reports which apply to businesses are required under Regulations 1161 and 1435; and that the reports are necessary for the health, safety or welfare of the people of the state.

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